In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 1060

EUCLID-TENNESSEE, INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

This case involves the applicability of § 382 of the Internal Revenue Code of 1954, which prohibits a corporation from carrying forward a previous year's net operating loss where there has been a more than 50 percent change in its stock ownership and it "has not continued to carry on a trade or business substantially the same as that conducted before any change" in ownership.

Until 1954 petitioner was engaged in the brewery business in Nashville, Tennessee. Because of substantial operating losses, it abandoned all brewery operations in 1954 and sold its brewery equipment. Petitioner's corporate life was continued to permit

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liquidation of its real estate. It is stipulated that petitioner had no intention of engaging in the active business of leasing real estate if it could be sold advantageously (R. 6a; Pet. A4).[1] Euclid-Tennessee, Inc., which was engaged in the business of selling and servicing construction equipment, became aware that petitioner had a large net operating loss carryover. Within a short time thereafter Euclid-Tennessee purchased all of petitioner's stock, and, through a series of tax-free transactions, Euclid-Tennessee's equipment business was transferred to petitioner, petitioner was renamed Euclid-Tennessee and moved to Old Euclid-Tennessee's plant site. Thereafter, petitioner operated the profitable equipment business received from Old Euclid-Tennessee and began renting to companies related to Old Euclid-Tennessee much of the real estate it had previously owned. The proceeds from the realty rentals were less than 1% of the proceeds from the equipment business.

Petitioner sought to deduct its previously incurred net operating losses (mainly from its discontinued brewery business) against the profits from the equipment business. The Commissioner disallowed the deductions.

It is conceded that there has been the requisite change in stock ownership necessary to invoke § 382. The sole dispute as to the applicability of § 382 is whether petitioner "continued to carry on a trade or business substantially the same as that conducted

[1] "R" references are to the record appendix to petitioner's brief in the court of appeals.

before" the change in ownership. The Tax Court found that petitioner's business after the change in ownership—*i.e.*, the equipment business—was not a continuation of a trade or business substantially the same as that carried on before—*i.e.*, the brewery business. The court of appeals affirmed (Pet. A1–A–16).

The decision below is correct, and there is no conflict between the circuits or other basis for review by this Court.

The record fully supports the concurrent finding of both courts below (Pet. A2, A8) that petitioner did not continue to carry on "substantially the same trade or business" after the change in its stock ownership, and that therefore the claimed net operating loss carryovers were barred by § 382(a)(1)(C). Petitioner discontinued its brewery business in 1954 and rented its real estate only in an effort to minimize its losses while winding up.[2] It was stipulated that petitioner never intended to engage in the regular and active leasing of real estate if the property could be sold advantageously (R. 6a; Pet. A4). After the change in ownership, petitioner rapidly minimized its real estate leasing activities, cutting its receipts almost in half in two years. Moreover, the character of the real estate leasing activities changed substantially. Petitioner changed its name, location,

[2] The taxpayer incurred losses from its brewery operations amounting to $42,092.37, $117,209.88, and $142,767.23 in 1952, 1953, and 1954, respectively (R, 6a). The taxpayer incurred losses from its rental activities of $6,023.44 and $5,112.50 in 1955 and 1956, respectively (Pet. A12).

officers, employees, customers and products; after the acquisition much of the property was leased to corporations which had been affiliated with Old Euclid (R. 13a–14a, 20a). At no time did the real estate leasing activities produce even 1% as much income as the equipment business (Pet. A5, fn. 4). The Tax Court found that petitioner's business prior to the ownership change was the manufacture and distribution of beer, not the leasing of its real property, and that petitioner's activity after the change did not represent a continuation of this business (Pet. A8, A10). The court of appeals properly affirmed (Pet. A3, A7) this factual determination as not clearly erroneous. *Commissioner* v. *Duberstein*, 363 U.S. 278.

The result is consistent with Section 382(a) and Congress' purpose in enacting it. Congress did not intend to permit a defunct company to assert that the profitless leasing on an interim basis of a parcel of real estate, which it was attempting to sell, was a business the continuance of which would permit the company's new owners to derive tax benefits by deducting losses sustained by the discontinued business against profits earned by a newly acquired business.[3]

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[3] S. Rep. No. 1622, 83d Cong., 2d Sess., p. 53 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4684) states that the Senate bill was designed to deal with those areas "in which abuse has most often arisen, that is, the purchase of the stock of a corporation with a history of losses for the purpose of using its loss carryovers to offset gains of a business unrelated to that which produced the losses." The Report further states (p. 285 (3 U.S.C. Cong. & Adm. News (1954), p. 4924))—

> If, as a result of such an * * * [ownership change], the corporation shifts from one type of business to another, discontinues any except a minor portion of its business,

Thus, to permit the continuance of insignificant real estate rental activities to serve as the basis for carrying over losses sustained by petitioner's old shareholders from the discontinued beer business against the profits realized by the new shareholders from the equipment business would fly in the face of both § 382's language and its purpose.

The instant decision does not conflict with *Maxwell Hardware Co.* v. *Commissioner,* 343 F. 2d 713 (C.A. 9), which held that the "continuity of business enterprise" test of *Lisbon Shops, Inc.* v. *Koehler,* 353 U.S. 382, 386, has no application under the 1954 Code. The court of appeals in the instant case did not invoke the *Libson Shops* test; the present decision rests solely on the applicability of Code § 382(a) as barring the claimed net operating loss carryover. The problem raised in *Maxwell Hardware, i.e.,* whether under the 1954 Code *Libson Shops* may independently bar a net operating loss carryover when § 382 is inapplicable, is not raised by the instant case.[4]

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changes its location, or otherwise fails to carry on substantially the same trade or business as was conducted before such an * * * [ownership change], then the condition in subparagraph (C) is met.

See also Section 1.382(a)-1(h), Treasury Regulations on Income Tax (1954 Code).

[4] The issue in *Maxwell Hardware* (whether there was more than a 50% change in stock ownership) was different from that presented by the instant case (whether there was a substantial change in the corporation's business). This presumably accounts for the absence of any reference to that case in the opinion below.

The taxpayer's reliance (Pet. A7–A8) on T.I.R. No. 773 (1965 C.C.H. Standard Federal Tax Reporter, par. 6751) in

Nor is the decision below in conflict with *Glover Packing Co. of Texas* v. *United States,* 328 F. 2d 342 (Ct. Cl.). There the Court of Claims held that the claimed loss carryover was barred under § 382(a)(1)(C) because the meat packing business conducted by the taxpayer after the stock ownership change was not substantially the same as either the meat packing business terminated almost five years previously or the subsequent rental activities.

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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asserting conflict with *Maxwell Hardware* apparently misconceives the tenor of that announcement. A careful reading of the full text of the T.I.R. indicates that the Internal Revenue Service (1) does not intend to follow *Maxwell* in "similar" cases; and (2) intends to urge the *Libson Shops* rationale only "where there has been both a 50 percent or more shift in the benefits of a loss carryover * * * and a change in business as defined in Section 382(a) and the Regulations thereunder"—*i.e.*, only where the limitation provisions of § 382(a) are otherwise applicable.

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